United States General Accounting Office

GAO

Report to the Congress



March 1991

# FINANCIAL AUDIT

# Savings Association Insurance Fund's 1989 Financial Statements

GAO

United States
General Accounting Office
Washington, D.C. 20548

Comptroller General
of the United States

B-114893

March 1, 1991

To the President of the Senate and the
Speaker of the House of Representatives

This report presents our opinion on the financial statements of the Savings Association Insurance Fund for the period August 9, 1989, through December 31, 1989, disclosing that the Fund's statements present fairly, in all material respects, its financial position and the results of its operations and cash flows. Our reports on the Fund's internal accounting controls and on its compliance with laws and regulations are also presented. We conducted our audit pursuant to the provisions of section 17(d) of the Federal Deposit Insurance Act, as amended (12 U.S.C. 1827(d)) and in accordance with generally accepted government auditing standards.

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) (Public Law 101-73), created the Savings Association Insurance Fund to provide deposit insurance to savings and loan institutions after the dissolution of the Federal Savings and Loan Insurance Corporation (FSLIC). The Fund is administered by the Federal Deposit Insurance Corporation. FIRREA also created the FSLIC Resolution Fund to assume the assets and liabilities resulting from FSLIC's resolution activity prior to January 1, 1989, and the Resolution Trust Corporation to resolve the problems of troubled institutions previously insured by FSLIC that are placed into conservatorship or receivership from January 1, 1989, until August 9, 1992. FIRREA provides the Resolution Trust Corporation (RTC) with $50 billion to resolve the problems of those institutions. After that date, the Savings Association Insurance Fund will be responsible for assisting troubled thrifts.

During fiscal years 1992 through 1999, the Fund will annually receive at least $2 billion. FIRREA requires the Department of the Treasury to pay to the Fund the difference between the assessments deposited in the Fund and $2 billion. In addition, Treasury is required to make annual payments to the Fund, not to exceed a total of $16 billion through fiscal year 2000, to ensure that the Fund has the minimum net worth specified in FIRREA. However, the Fund's ability to maintain adequate capital levels and provide insurance protection to depositors is directly dependent on the number and cost of savings institutions that it must resolve. Our report discusses various estimates of the number and cost of savings institutions that will require resolution after August 9, 1992; the availability of funds necessary for their resolution; and the resulting impact on the Savings Association Insurance Fund. According to one

estimate, the Fund may confront significant costs, perhaps even a backlog of failed institutions, when it assumes resolution responsibility. Under these conditions, the Fund may be insolvent, or close to it, when it assumes the duties of deposit insurer in 1992.

We are sending copies of this report to the Chairmen of the Senate Committee on Banking, Housing and Urban Affairs and the House Committee on Banking, Finance and Urban Affairs; the Secretary of the Treasury; the Chairman of the Federal Housing Finance Board; the Director of the Office of Management and Budget; and the Director of the Office of Thrift Supervision.

Charles A. Bowsher
Comptroller General
of the United States

# Contents



**Abbreviations**

| | |
|---|---|
| CBO | Congressional Budget Office |
| FDIC | Federal Deposit Insurance Corporation |
| FICO | Financing Corporation |
| FIRREA | Financial Institutions Reform, Recovery, and Enforcement Act |
| FSLIC | Federal Savings and Loan Insurance Corporation |
| OTS | Office of Thrift Supervision |
| REFCORP | Resolution Funding Corporation |
| RTC | Resolution Trust Corporation |

GAO

**United States**
**General Accounting Office**
**Washington, D.C. 20548**

**Comptroller General**
**of the United States**

B-114893

To the Board of Directors
Federal Deposit Insurance Corporation

We have audited the accompanying statement of financial position of the Savings Association Insurance Fund as of December 31, 1989, the related statement of income and fund balance, and the statement of cash flows for the period August 9, 1989, through December 31, 1989. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit. In addition to this report on our audit of the Fund's 1989 financial statements, we are reporting on our consideration of the Fund's internal control structure and on its compliance with laws and regulations.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Savings Association Insurance Fund as of December 31, 1989, and the results of its operations and its cash flows for the period then ended, in conformity with generally accepted accounting principles.

As discussed in note 1, the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) was enacted on August 9, 1989. FIRREA responded to the savings and loan industry crisis and the mounting losses of the industry's insurer by abolishing the Federal Savings and Loan Insurance Corporation (FSLIC) and transferring its functions to several newly established entities. FSLIC's insurance function was transferred to the Savings Association Insurance Fund, which is administered by the Federal Deposit Insurance Corporation (FDIC). FIRREA created the FSLIC Resolution Fund to assume the assets, debts, obligations, contracts, and other liabilities resulting from FSLIC's resolution activity prior to January 1, 1989. FDIC is responsible for administering the FSLIC Resolution Fund to ensure that its assets are sold and liabilities paid. FIRREA

also created the Resolution Trust Corporation (RTC) to resolve the problems of failed institutions previously insured by FSLIC that are placed into conservatorship or receivership from January 1, 1989, until August 9, 1992. After that date, the Savings Association Insurance Fund will be responsible for assisting and resolving troubled thrifts.

FIRREA provided various mechanisms for funding the entities it established. The FSLIC Resolution Fund will pay its liabilities with revenue from several different sources, including recoveries from the sale of assets FSLIC acquired in assisting failed thrifts and insurance premiums assessed against savings institutions until the end of 1991. Any additional funds needed are to be provided by the Department of the Treasury.

FIRREA provided RTC with $50 billion to resolve failed savings institutions and to pay its administrative expenses. However, current resolution cost estimates by RTC and its Oversight Board indicate that at least another $50 billion will be needed. On January 23, 1991, the Oversight Board appeared before the Senate Committee on Banking, Housing and Urban Affairs to request an additional $30 billion for resolutions through fiscal year 1991. Without additional funding, RTC is expected to stop closing and selling institutions by the end of February 1991.

For the Savings Association Insurance Fund, FIRREA provided several revenue sources, but none will supply significant revenue to the Fund prior to fiscal year 1992.[1] Until then, the FSLIC Resolution Fund has been charged with paying the Savings Association Insurance Fund's administrative and supervisory expenses. Beginning with insurance premiums assessed after October 1, 1991, however, the Fund will receive that portion of assessments not required to pay interest on bonds sold to recapitalize FSLIC. Further, to the extent that assessments deposited in the Fund do not total $2 billion a year, Treasury is required to fund the difference for each of the fiscal years 1992 through 1999. Treasury also is required to pay the Fund any additional amounts necessary to ensure

[1]Through December 1991, the Savings Association Insurance Fund will not receive any insurance premium assessment proceeds; after that date, the Fund will receive part of the assessment amounts. The Financing Corporation (FICO), which was established in 1987 by Public Law 100-86 to issue bonds for recapitalizing FSLIC, has first claim on insurance premium assessment funds for payment of interest on its bonds. FICO's claim will continue until the recapitalization bonds mature. In addition, the Resolution Funding Corporation (REFCORP), established by FIRREA to provide $30 billion of funding to RTC, was entitled to insurance premium assessment funds if needed to defease bond principal. REFCORP issued the last bonds in early January 1991 and will therefore have no further claim to assessments. Finally, the FSLIC Resolution Fund is entitled through December 1991 to any assessment income not taken by FICO and REFCORP.

that the Fund has the annual minimum net worth specified in FIRREA during fiscal years 1992 through 2000. However, the cumulative amount of these net worth payments cannot exceed $16 billion.

Clearly, the Fund's ability to provide protection to depositors is dependent on the number and cost of savings institutions that fail and must be resolved after August 9, 1992. The following sections of this report discuss various estimates of future savings institution failures, the source and availability of funds necessary for their resolution, and the resulting impact on the Savings Association Insurance Fund.

## Estimates of Future Thrift Failures Vary

With the passage of FIRREA, the thrift industry has been divided into two distinct groups: institutions in conservatorship under government control and those remaining in the private sector. In May 1990, the Office of Thrift Supervision (OTS) released the results of its study of the industry and divided the remaining private sector thrifts into four groups based on their ability to meet capital standards, their prospects for future viability, and the results of supervisory/regulatory examinations.[2] Preliminary data for the second quarter of 1990 indicates that private sector thrifts number approximately 2,450 institutions and are grouped as follows.

- Category I institutions comprise nearly half the private sector industry and hold 35 percent of its assets. This group is considered healthy and well capitalized. These institutions have a composite supervisory rating of 1 or 2 and are allowed reasonable flexibility to engage in activities without excessive regulation as long as they keep their strong capital and low risk positions.
- Category II institutions, the "near-healthy," total approximately one-quarter of the industry and hold 33 percent of its assets. These institutions currently meet or are expected to meet capital requirements. Category II institutions have a composite supervisory rating of 2 or 3 and are also allowed reasonable flexibility as long as capital continues to improve and risk remains low.
- Category III institutions, about one-eighth of the total institutions and holding 16 percent of their assets, are considered "troubled," with poor

[2]OTS has developed a rating system that reflects its evaluation of each institution's financial condition, compliance with laws and regulations, and overall operating soundness. Each institution is assigned a uniform composite rating based on an OTS evaluation. This overall rating is expressed through use of a numerical scale of "1" through "5" in ascending order of supervisory concern; "1" indicates the highest rating and least degree of concern, while "5" is the lowest rating and therefore highest degree of concern

earnings and low capital. Many institutions in this category failed to meet the new OTS capital requirements and had to submit capital plans for approval. The OTS composite supervisory rating is usually a 3 or 4 and, as a result, these institutions are subject to more regulation and are tracked very closely to ensure compliance with approved capital plans. The future viability of Category III institutions is tenuous.

- Category IV institutions, nearly one-eighth of the total with 15 percent of the assets, are given little or no chance of continuing in the private sector. These institutions have composite supervisory ratings of 5, the worst possible. Since OTS is virtually certain that these institutions will be transferred to RTC, its overriding regulatory concern is to reduce their eventual resolution costs.

In addition to the four OTS private sector categories, a separate group of savings institutions is currently being operated under government control while awaiting resolution. These conservatorship institutions were transferred to RTC because they had negative capital, were consistently unprofitable, and/or were operating in an unsafe and unsound manner. While under RTC management, conservatorships are operated under strict policies regarding asset sales, high-risk investments, and high-cost funds.

By grouping institutions according to their likelihood of becoming resolution candidates, OTS has created a useful tool for defining the size and composition of the potential resolution universe and for producing comparable cost estimates. It is important to remember, however, that the condition of the savings industry is not static. Institutions will, and have, moved from one category to another based on new quarterly financial data and on RTC resolution activity.

On May 23, 1990, the Chairman of the RTC Oversight Board testified before the Senate Committee on Banking, Housing, and Urban Affairs concerning the expected number and costs of RTC resolutions. Using the OTS categories, the Board developed a range of loss estimates from $89 billion to $132 billion on a present value basis.[3] The Board's lower estimate reflects average expected losses of approximately 14 percent on sales of assets acquired in resolving the approximately 700 institutions in conservatorship and in OTS Category IV—those deemed likely to be transferred to RTC. The Board's high estimate is based on average

[3] In its January 23, 1991, appearance before the Senate Banking Committee, the Oversight Board stated that the $89 billion to $132 billion range estimates remain valid. However, the recent downturn in the economy and the crisis in the Persian Gulf make the high end of the range more likely.

expected losses of 22 percent on asset sales in the institutions included above as well as in the more than 300 troubled institutions included in OTS Category III.

According to the Oversight Board, some of the thrifts included in its estimate were originally expected to become the responsibility of the Savings Association Insurance Fund; however, these cases are failing sooner than expected and will probably become RTC's responsibility. The Board stated that failures will probably not surpass the 1,000 predicted in its testimony and that losses are unlikely to exceed the $132 billion estimated. Thus, the Board predicted that RTC will resolve all expected future savings institution failures and absorb all of the related costs.

In conjunction with our testimony before the House Committee on Ways and Means in September 1990,[4] we obtained and reviewed the Oversight Board's current methodology and assumptions for developing its range of resolution cost estimates. On the basis of our work, we concluded that the Board's methodology was standardized and consistent and that the resulting cost estimates were reasonable. However, the Board has agreed with us that these estimates are subject to change if underlying factors change. This could result in more institutions failing or in greater losses on failed institutions' assets.

In June 1990, the Congressional Budget Office (CBO) released its economic and budget projections for the 5-year period beginning October 1, 1991, and estimated that nearly 1,700 savings associations are likely to fail. CBO also estimated that a significant portion of those failures will occur after 1992 and therefore will have to be resolved by the Savings Association Insurance Fund.

For resolutions that will be the responsibility of RTC, CBO's projections are similar to those of the Oversight Board. CBO estimates that RTC will resolve 925 institutions at a cost, if resolved today, of $90 billion to $130 billion. Most of these institutions are currently in conservatorship or in the lowest groups (Categories III and IV) identified by OTS.

However, CBO also identified nearly 800 savings associations that are currently solvent based on the book value of their assets but would become insolvent if their assets were written down to reflect CBO estimated market prices. Most of these institutions are OTS Category II

[4] Resolving Failed Savings and Loan Institutions: Estimated Costs and Additional Funding Needs (GAO/T-AFMD-90-32, September 19, 1990).

thrifts, those that meet or are expected to meet capital standards, but some are from Category I, institutions considered healthy and well capitalized. Because they have capital now and can absorb some losses, CBO does not expect these institutions to require resolution before 1992. CBO estimates their resolution will cost the Savings Association Insurance Fund approximately $35 billion on a present value basis.

We reviewed CBO's estimates and found that for those institutions expected to become RTC's responsibility prior to 1992, we agreed with CBO's assumptions and found the resulting cost range to be reasonable. We found CBO's cost estimates for institutions projected to fail after 1992 more uncertain, however, due to the extended time period over which the additional 800 institutions are expected to fail and their current positive capital levels. But CBO's estimates have pointed to the possibility that the Savings Association Insurance Fund may confront significant costs, perhaps even a backlog of failed institutions, when it assumes resolution responsibility.

## unding Sources May e Inadequate

Although FIRREA provided the Fund with several revenue sources, only two sources will provide the significant amounts that may be required for resolution activity—insurance premiums and Treasury payments. Funds from these sources may be used to pay the Savings Association Insurance Fund's obligations and establish a minimum insurance fund balance. During fiscal years 1992 through 1999, FIRREA requires Treasury to pay the Fund annually the difference between $2 billion and premium assessment income deposited in the Fund. In addition, Treasury is required to make annual payments necessary to ensure that the Fund has the minimum net worth specified in FIRREA, ranging from zero during fiscal year 1992 to $8.8 billion during fiscal year 2000. The cumulative amount of these net worth payments cannot exceed $16 billion.

Assuming optimistic deposit growth rates of 5 percent a year and assuming application of the regular insurance premium assessment rates stated in FIRREA, the assessments deposited in the Fund will not exceed $2 billion in any one year. Thus, the maximum amounts from assessments and Treasury payments that the Fund will receive under the statutory scheme through 1999 will be $32 billion. Even assuming use of the accelerated insurance premium assessment rates allowable after 1995, the Fund's income for the 8-year period is unlikely to exceed $34 billion. Whether either amount will be sufficient to pay its obligations and

achieve the net worth goals in FIRREA will depend on the resolution demands the Fund faces in the future.

If the Oversight Board's resolution projections prove correct and if RTC is given the funds needed to resolve all of the 700 to 1,000 expected future savings institution failures, the outlook for building an adequately capitalized fund is promising. The Savings Association Insurance Fund would not face an immediate or significant case resolution liability and could use its assessments and Treasury payments to increase its net worth beyond the minimum required. The Fund would then be able to provide a strong deposit insurance base to meet the needs of the savings and loan industry.

If, however, CBO's projections prove true and an additional 800 institutions fail, the Savings Association Insurance Fund will not have the resources to cover expected resolution costs. The present value of $34 billion in cash, the maximum expected to be available for resolutions over 8 years, falls short of CBO's estimated $35 billion present value resolution cost. Depending on the timing of failures, the Fund might have to recognize most or all of the expected resolution costs as soon as it accepts resolution responsibility in August 1992. Under these conditions, the Savings Association Insurance Fund may be close to, if not actually, insolvent when it assumes all the duties of deposit insurer.

Because of the uncertainties inherent in projecting so far into the future, possible resolution costs and the future viability of the deposit fund are issues that cannot be adequately addressed at present. However, we will be monitoring future events, evaluating their effects on the Savings Association Insurance Fund, and reporting our findings as part of future financial statement audits.

Charles A. Bowsher

Charles A. Bowsher
Comptroller General
of the United States

July 31, 1990

# Report on Internal Control Structure

We have audited the financial statements of the Savings Association Insurance Fund for the period August 9, 1989, through December 31, 1989, and have issued our opinion thereon. This report pertains only to our study and evaluation of the Federal Deposit Insurance Corporation's (FDIC) internal control structure as it relates to the Savings Association Insurance Fund for the period ended December 31, 1989.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

In planning and performing our audit of the financial statements of the Savings Association Insurance Fund for the period ended December 31, 1989, we considered its internal control structure in order to determine our auditing procedures for the purposes of expressing our opinion on the financial statements and not to provide assurance on the internal control structure.

FDIC's management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the internal control structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For purposes of this report, we have classified FDIC's significant internal control structure policies and procedures into the following categories:

- revenue, consisting of policies and procedures over assessments, cash receipts, and investment activities, and
- expenditures, consisting of policies and procedures over cash disbursements.

For both internal control structure categories listed above, we obtained an understanding of the design of the relevant policies and procedures, determined whether they have been placed in operation, and assessed the associated control risk. We performed limited tests of control procedures for assessments and cash disbursements. However, we found it more efficient to rely solely on substantive audit tests for investment and cash receipts activities. For all categories, we performed audit tests to substantiate account balances associated with each control category. Such tests can also serve to identify weaknesses in the internal control structure.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operation that we consider to be material weaknesses as defined above.

However, we noted certain matters involving the internal control structure and its operations that do not affect the fair presentation of the Savings Association Insurance Fund's financial statements but which nevertheless warrant management's attention. We reported these matters to FDIC's management as they were discovered.

# Report on Compliance With Laws and Regulations

We have audited the financial statements of the Savings Association Insurance Fund for the period August 9, 1989, through December 31, 1989, and have issued our opinion thereon. This report pertains only to our review of the Federal Deposit Insurance Corporation's (FDIC) compliance with laws and regulations as they relate to the Savings Association Insurance Fund for the period ended December 31, 1989.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

FDIC's management is responsible for compliance with laws and regulations applicable to the Savings Association Insurance Fund. As part of obtaining reasonable assurance as to whether the financial statements were free of material misstatements, we selected and tested transactions and records to determine FDIC's compliance with certain provisions of the Federal Deposit Insurance Act (12 U.S.C. 1811 et seq.) and title IV of the National Housing Act (12 U.S.C. 1724-1730), as amended, which, if not complied with, could have a material effect on the Savings Association Insurance Fund's financial statements. We also tested compliance with provisions of the Prompt Payment Act (31 U.S.C. 3901-3906) and such other laws and regulations which we considered pertinent. However, it should be noted that our objective was not to provide an opinion on overall compliance with such provisions. Because of the limited purpose for which our tests of compliance were made, the laws and regulations tested did not cover all legal requirements with which FDIC has to comply.

The results of our tests indicate that with respect to the items tested, FDIC complied, in all material respects, with those provisions of laws and regulations that could have a material effect on the Fund's financial statements. With respect to transactions not tested, nothing came to our attention that caused us to believe that FDIC had not complied, in all material respects, with those provisions.

# Financial Statements

## Statement of Financial Position

**As of December 31, 1989**
**(In thousands)**

| | |
|---|---|
| **Assets** | |
| Cash and cash equivalents | $ -0- |
| Due from FSLIC Resolution Fund (Note 1) | 1,120 |
| SAIF member exit fees receivable, net (Note 3) | 3,151 |
| Other assets | 1,035 |
| | **$ 5,306** |
| **Liabilities and the Fund Balance** | |
| Accounts payable, accrued liabilities and other | 2,153 |
| SAIF member exit fees held in reserve (Note 3) | 3,151 |
| Fund Balance | 2 |
| | **$ 5,306** |

See accompanying notes

## Statement of Income and the Fund Balance

**For the period from Inception (August 9, 1989) through December 31, 1989**
**(In thousands)**

| | |
|---|---|
| **Revenue** | |
| Entrance fee revenue (Note 3) | $ 2 |
| **Total Revenue** | **2** |
| **Expenses** | |
| Administrative operating expenses | 5,602 |
| **Total Expenses** | **5,602** |
| **Loss before Funding Transfer** | **(5,600)** |
| Funding Transfer from FSLIC Resolution Fund (Note 1) | 5,602 |
| **Net Income** | **2** |
| **Fund Balance - August 9** | **-0-** |
| **Fund Balance - December 31** | **$ 2** |

See accompanying notes

## Statement of Cash Flows

**For the period from Inception (August 9, 1989) through December 31, 1989**
**(In thousands)**

| | |
|---|---|
| **Cash Flows From Operating Activities:** | |
| Cash inflows from: | |
| Transition assessment principal proceeds (Note 4) | $ 98,827 |
| Interest on transition assessment principal proceeds | 1,914 |
| FRF funding transfer | 4,482 |
| Cash outflows for: | |
| Transition assessment payment transferred to FRF | 100,672 |
| Administrative operating expenses | 4,551 |
| **Net Cash Provided By Operating Activities** | **-0-** |
| **Cash Flows From Investing Activities** | **-0-** |
| **Cash Flows From Financing Activities** | **-0-** |
| **Cash and Cash Equivalents - August 9** | **-0-** |
| **Cash and Cash Equivalents - December 31** | **$ -0-** |

See accompanying notes

**DECEMBER 31, 1989**

**1. Impact of FIRREA Legislation:**

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) became public law on August 9, 1989. The primary purpose of the legislation was to reform, recapitalize, and consolidate the federal deposit insurance system so as to restore the public's confidence in the savings and loan industry and to ensure a safe and stable system of affordable housing finance through major regulatory reforms, strengthened capital standards and safeguards for the disposal of recoverable assets. FIRREA abolished the Federal Savings and Loan Insurance Corporation (FSLIC) and the Federal Home Loan Bank Board (FHLBB). Their functions were transferred, in a prescribed manner, to the Federal Deposit Insurance Corporation (FDIC), the Office of Thrift Supervision, the Federal Housing Finance Board, and the Resolution Trust Corporation (RTC).

Under FIRREA, the FDIC became the administrator of two separate and distinct insurance funds: the Bank Insurance Fund (BIF; formerly the Deposit Insurance Fund) which insures the deposits of all BIF member banks, and the Savings Association Insurance Fund (SAIF) which insures the deposits of all SAIF member savings associations (formerly a function of the FSLIC). Both insurance funds are maintained separately to carry out their respective legislative mandates, with no commingling of assets or liabilities. The FSLIC Resolution Fund (FRF), a third separate fund under FDIC management, the SAIF and the RTC replaced the FSLIC in case resolution activities.

The Resolution Funding Corporation was established by FIRREA to provide funds to the RTC to enable the RTC to carry out its mandate. The Financing Corporation (established under the Competitive Equality Banking Act of 1987) is a mixed-ownership government corporation whose sole purpose is to function as a financing vehicle for the FRF (formerly the FSLIC).

*Creation and Purpose of the SAIF.* FIRREA authorized and directed the FDIC to establish and manage a separate insurance fund to be known as the Savings Association Insurance Fund. Savings associations which were insured by the FSLIC prior to FIRREA automatically became insured depository institutions and members of the SAIF without application or approval. The primary mission and purpose of the SAIF is to insure the deposits and to protect the depositors of SAIF insured savings associations.

The SAIF began operations with no assets or liabilities. All assets and liabilities of the FSLIC existing on August 8, 1989 were transferred to the FSLIC Resolution Fund, except for certain liabilities which were assumed by the Resolution Trust Corporation. Any administrative facilities and supplies remaining after dissolution of the FRF will be transferred to the SAIF.

Currently the SAIF is only financially responsible for the resolution of newly established insured depository institutions that become members of the SAIF after August 8, 1989. The Resolution Trust Corporation will manage and resolve all thrifts that were previously insured by the FSLIC and for which a conservator or receiver is appointed during the period January 1, 1989 through August 8, 1992. The SAIF will be financially responsible for all member depository institutions placed in conservatorship or receivership after August 8, 1992.

Beginning on August 9, 1989 and ending on September 30, 1991, the administrative and supervisory expenses incurred by the SAIF will be the funding responsibility of the FSLIC Resolution Fund. Such expenses will have priority over other obligations of the FRF. Funding by the FRF is effective as expenses are recognized by the SAIF. As of December 31, 1989, the FRF had recognized $5,602,000 in funding transfers to the SAIF, of which $1,120,000 remained unpaid.

*Source of Funds.* FIRREA provides seven distinct funding sources for the SAIF: (1) FRF funding of administrative and supervisory expenses, as discussed above; (2) SAIF member assessments available which are not required for the Financing Corporation, the Resolution Funding Corporation, or the FSLIC Resolution Fund; (3) U. S. Treasury payments for the amount, if any, by which $2,000,000,000 exceeds the amount of assessments deposited in the SAIF for each of the fiscal years 1992 through 1999; (4) U. S. Treasury payments for any additional amounts which may be necessary to ensure that the SAIF has the minimum net worth set by FIRREA for each of the fiscal years 1992 through 2000; (5) discretionary payments by the RTC; (6) Federal Home Loan Bank borrowings; and (7) U. S. Treasury borrowings up to $5,000,000,000.

Other miscellaneous sources of SAIF revenue include insurance fees from new SAIF members, entrance fees from insured depository institutions involved in allowable conversion and transfer transactions between the Bank Insurance Fund and the SAIF, and investment revenue earned on assessment collections and such fees.

**2. Summary of Significant Accounting Policies:**

*Assessment Revenue Recognition.* The SAIF recognizes as assessment revenue only that portion of SAIF member assessments due that is not required for the Financing Corporation, the Resolution Funding Corporation, or the FSLIC Resolution Fund.

*Litigation Losses.* The SAIF accrues as a charge to current period income an estimate for probable loss from litigation against the SAIF. The FDIC Legal Division recommends these estimated losses on a case-by-case basis. However, as of December 31, 1989, no litigation is pending against the SAIF.

*Depreciation.* The cost of furniture, fixtures, and equipment is expensed at time of acquisition. This policy is a departure from generally accepted accounting principles; however, capitalizing these expenditures would not be cost-beneficial to SAIF.

*Cash Equivalents.* The SAIF considers cash equivalents to be short-term, highly liquid investments with original maturities of three months or less. This includes the purchase of one-day Special Treasury Certificates. However, as of December 31, 1989, these cash equivalents amounted to $ -0-.

**3. Entrance and Exit Fees:**

In accordance with FIRREA provisions, the SAIF will receive entrance and exit fees for conversion transactions in which an insured depository institution converts from the Bank Insurance Fund to the SAIF (resulting in an entrance fee) or from the SAIF to the Bank Insurance Fund (resulting in an exit fee). Interim regulations approved by the FDIC Board of Directors and published in the Federal Register on March 21, 1990 expanded the FIRREA provisions by directing that exit fees paid to SAIF be held in a reserve account until such time as the FDIC and the Secretary of the Treasury determine that it is no longer necessary to reserve such funds for the payment of interest on the obligations of the Financing Corporation.

The SAIF records entrance fees as a receivable and related revenue once the BIF-to-SAIF conversion transaction is consummated. However, due to the requirement that SAIF exit fees be held in a reserve account, thereby restricting the SAIF's use of such proceeds, the SAIF does not recognize exit fees as revenue. Instead, the SAIF recognizes the consummation of a SAIF-to-BIF conversion transaction by establishing a receivable from the institution and an identical liability/reserve account to recognize the probable obligation to the Financing Corporation. As exit fee proceeds are received, the receivable is reduced while the liability remains pending the determination of funding requirements for interest payments on the Financing Corporation's obligations.

Within specified parameters, the interim regulations allow an acquiring institution to pay its entrance/exit fees due, interest free, in equal annual installments over a period of not more than five years. When an institution elects such a payment plan, the SAIF records the entrance and exit fee receivable at its present value.

As of December 31, 1989, the exit fees have been recorded in the accounting records at a net amount of $3,151,000 ($3,716,000 less an unamortized discount of $565,000); the entrance fees have been recorded in the accounting records at $2,000.

**4. Assessments**:

The Federal Deposit Insurance (FDI) Act, as amended by FIRREA, directs that the FDIC set assessment rates for SAIF members annually in accordance with the legislatively mandated rates against a member's average assessment base.

The FDI Act also provides for an assessment credit to SAIF members when the Board of Directors determines that the SAIF reserve ratio is expected to exceed the designated reserve ratio in the succeeding year, after taking into account expected expenses and revenues. The FDI Act defines the SAIF designated reserve ratio as (i) 1.25 percent of estimated insured deposits; or (ii) a higher percentage, not to exceed 1.50 percent, as determined by the Board of Directors to cover expected risks of future losses.

The assessment rate set for 1990 is 0.208 percent. Based on the present and projected status of the SAIF, and anticipated expenses and revenue for the next year, the reserve ratio is not expected to exceed the designated reserve ratio. Therefore, savings associations will not receive an assessment credit in 1990.

*Secondary Reserve Offset.* Title II, Section 208 of FIRREA authorizes insured savings associations to offset against any assessment premiums their pro rata share of amounts that were previously part of the Federal Savings and Loan Insurance Corporation's "Secondary Reserve." FIRREA limits the allowable offset to 20 percent of an association's remaining pro rata share for any calendar year beginning before 1993. After calendar year 1992, there is no limitation on the remaining offset amount.

The Secondary Reserve offset serves to reduce the gross SAIF member assessments due, thereby reducing the assessment premiums available to the Financing Corporation, the Resolution Funding Corporation, the FSLIC Resolution Fund, and the SAIF.

*Transition Assessment.* In September 1989, the FDIC allowed for a one-time, transition assessment against SAIF members to change such members' premium assessment due dates to a semiannual basis. This special assessment available from SAIF members totalled $393,827,000, of which $295,000,000 was claimed by the Financing Corporation for debt servicing needs. Remaining funds of $98,827,000 were deposited in the SAIF until the proper owner of the funds could be determined. These funds, in addition to interest earned thereon, were subsequently allocated to the FSLIC Resolution Fund in the absence of assessment authority by the Resolution Funding Corporation on the transition assessment date. As of December 31, 1989, $120,000 in interest remained to be transferred to the FSLIC Resolution Fund in 1990.

As discussed above, the September 1989 transition assessment against SAIF members yielded the following results (in thousands):

| | |
|---|---|
| Gross SAIF member assessments due | $ 639,565 |
| Less: Secondary Reserve offset | (64,982) |
| Other adjustments/credits | (180,756) |
| **Net SAIF member assessments available** | **393,827** |
| Less: FICO assessment | (295,000) |
| REFCORP assessment | -0- |
| **Principal funds provided to the FRF** | **$ 98,827** |

**5. Pension Plan:**

The FDIC's eligible employees assigned to the SAIF are covered by the Civil Service Retirement and Disability Fund. Matching employer contributions provided by the SAIF for all eligible employees were approximately $288,000 for the period from inception (August 9, 1989) through December 31, 1989.

Although the SAIF contributes a portion of the pension benefits for eligible employees and makes the necessary payroll withholdings from them, the SAIF does not account for the assets of the Civil Service Retirement and Disability Fund, nor does it have actuarial data with respect to accumulated plan benefits or the unfunded liability relative to its eligible employees. These amounts are reported by the U. S. Office of Personnel Management (OPM) and are not allocated to the individual employers. OPM also accounts for all health and life insurance programs for retired eligible employees.

**6. Commitments:**

The SAIF is currently sharing in the FDIC lease of office space to accommodate its staff. Lease commitments for office space total $1,249,000 for future years. Lease space expense for the period from inception (August 9, 1989) through December 31, 1989 amounted to $25,000. Expected leased space fees for future years are as follows (in thousands):

| 1990 | 1991 | 1992 | 1993 | 1994 | 1995/Thereafter |
|---|---|---|---|---|---|
| $338 | $303 | $264 | $182 | $136 | $26 |

**7. Supplementary Information Relating to the Statement of Cash Flows (in thousands):**

*Reconciliation of net income to net cash provided by operating activities for the period from inception (August 9, 1989) through December 31, 1989*

| | |
|---|---|
| **Net Income** | **$ 2** |
| Adjustments to reconcile net income to net cash provided by operating activities: | |
| Increase in accounts payable, accrued liabilities and other | 2,153 |
| Due from FSLIC Resolution Fund (funding transfer) | (1,120) |
| (Increase) in other assets | (1,035) |
| **Net cash provided by operating activities** | **$ -0-** |